BAY STATE GAS COMPANY

PREFILED TESTIMONY OF FRANCISCO C. DAFONTE

Q. Please state your name and business address.

A. Francisco C. DaFonte. My business address is 300 Friberg Parkway, Westborough, MA 01581.

Q. By whom are you employed and in what capacity?

A. I am a Director, Energy Supply Services for Bay State Gas Company ("Bay State" or "the Company") and Northern Utilities, Inc. ("Northern").

Q. What are your responsibilities as Director, Energy Supply Services?

A. I am responsible for planning, managing and optimizing the gas supply portfolio for Bay State.

Q. Please summarize your educational background and professional experience.

A. I received a Bachelor of Science Degree in Mathematics from the University of Massachusetts at Amherst in 1985. I was subsequently hired by Commonwealth Gas Company, where I was employed primarily as a supervisor in gas dispatch and gas supply planning for nine years. In 1994, I joined Bay State and its affiliate Northern as a Gas Resource Marketing Analyst. In May 1996, I was promoted to Director of Gas Control. In July 2001 I was given my current title of Director, Energy Supply Services.

Q. Are you a member of any professional organizations?

A. Yes. I am a member of the New England Gas Association, the American Gas Association, the National Energy Services Association and the New England Canada Business Council.

Q. Have you previously testified before any regulatory or governmental bodies?

A. Yes, I have testified in a number of proceedings before the Commonwealth of Massachusetts Department of Telecommunications and Energy ("Department" or

"DTE"), the State of New Hampshire Public Utilities Commission, the State of Maine Public Utilities Commission and the Federal Energy Regulatory Commission

Q. What is the purpose of your testimony in this proceeding?

A. The purpose of my testimony in this proceeding is to demonstrate that Bay State's selection of a gas supply agreement and associated agreements to replace the current Boundary Gas Inc. ("BGI") supply that will expire in January 2003 was undertaken in a manner consistent with Department precedent. Bay State employed its decision-making process to arrive at the best decision for its customers based on all alternatives available to it at the time. Bay State's planning process, which has been reviewed and approved by the Department, utilized appropriate least-cost planning techniques and evaluated the price and non-price characteristics of each supply option prior to selecting EnCana Corporation ("EnCana") as the replacement supplier for its current BGI contract, which was approved by the Department in DPU 94-16.

My testimony provides a description of each of the agreements that comprise the Boundary replacement supply including the Gas Sales Agreement ("GSA") with EnCana (see Exhibit FCD-1), the Agency Agreement ("AA") between Bay State and Northeast Gas Markets, LLC ("NEGM") (see Exhibit FCD-2), and the Management Services Agreement ("MSA") between Bay State and NEGM (see Exhibit FCD-3). Further, I will provide an overview of the Boundary Gas Renewal Project ("the Project") including the Boundary background, the Project working group and the comprehensive RFP process that resulted in Bay State's decision to enter into a twenty-six (26) month supply arrangement with EnCana. In addition, I will describe how Bay State's EnCana decision is consistent with the Department's precedent and standard of review for contracts to be applied in this case. Finally, I will present a summary of conclusions.

GSA, AA and MSA Agreements

Q. Please describe the GSA.

A. The GSA between Bay State and EnCana has an initial term commencing on January 15, 2003 and ending on February 1, 2003 in order to take into account the mid-month expiration of the current Boundary contract. The primary term of the GSA has a commencement date of February 1, 2003 and an expiration date of April 1, 2005. The MDQ or daily contract quantity will be 10,471 Dth/day, with Bay State retaining the flexibility to reduce the MDQ by as much as 100% no later than five (5) business days prior to the beginning of the next month. The pricing for the initial term is tied to the "Midpoint Price" as set forth in the *Daily Price Survey* published by GAS DAILY for deliveries at Niagara, and is shown in Section 1.1 (Confidential) of the GSA. The pricing for the primary term is also tied to the *Gas Daily Price Guide* published monthly by GAS DAILY for deliveries at Niagara in the applicable month and is shown in Section 1.1 (Confidential) of the GSA. NEGM will act as the administrative agent for Bay State as well as for all the other LDCs designated in the GSA.

The AA is entered into by and among NEGM, Bay State and those other LDCs designated in the agreement. The AA authorizes NEGM to act on each customer's behalf as administrative agent for all purposes under and with respect to the individual GSA with EnCana, including, submitting nominations to EnCana on behalf of each customer, receiving invoices and making payments on behalf of each customer, declaring, or receiving notice of, *Force Majeure* on behalf of each customer, negotiating or determining an Alternate Index on behalf of each customer, and carrying out all other necessary actions related to the GSA, including, preparing and filing U.S. Customs forms and payments and other operational reports as may be required by regulatory agencies. See, FCD-2.

The MSA is entered into by and among NEGM, Bay State and those other

LDCs designated in the agreement. The MSA details all services to be rendered by NEGM for the express purpose of acting as administrative agent for all customers designated in the agreement. As compensation for the services rendered by NEGM under the MSA, each customer shall pay to NEGM each month a fee equal to the product of three components; a $0.0128 per Dth administration rate, the MDQ under its respective GSA, and the number of days in such month, without regard to actual quantities of gas delivered to such customer for that month. See, FCD-3.

<u>Boundary Gas Renewal Project</u>

Q. Please provide the background for Boundary Gas, Inc.

A. Boundary Gas, Inc. was formed in 1980 as a consortium of local distribution companies ("LDCs") in the U.S. Northeast to facilitate the procurement of incremental supplies of natural gas to meet market growth. It was the first direct purchase venture by gas distribution companies in the United States and was designed to overcome the region's inability to obtain adequate incremental gas supplies from traditional pipeline suppliers to meet steadily growing requirements.

Natural gas began flowing under the first Boundary contract to four LDCs in New York and New Jersey in 1984. Full contract deliveries to fifteen LDCs in New York, New Jersey and New England commenced in January 1988. The existing contract is structured so that gas is delivered from Canada to the US at the Niagara Falls import point. BGI purchases and resells the gas to its Northeast customer group LDCs [1] at that point. These LDCs hold individual direct transportation capacity contracts on Tennessee Gas Pipeline ("TGP") that align with their respective portions of

[1] Brooklyn Union Gas, New Jersey Natural Gas, Connecticut Natural Gas, Consolidated Edison, National Fuel, Boston Gas Company, Energy North, Essex County Gas, Valley Gas, Berkshire Gas Company, Fitchburg Gas and Electric Company, Bay State Gas Company, and Northern Utilities, Inc.

the BGI supply contract. Currently, 100% of the gas volume required by BGI is supplied by Mirant Canada Gas Marketing (formerly TransCanada Gas Services). NEGM, a Beverly, Massachusetts – based project development and contract management firm, manages all aspects of BGI and the BGI gas supply contract, including gas operations, treasury, invoicing, renegotiations and regulatory matters.

Q. Please describe the Boundary Renewal Working Group.

A. In the spring of 2001 BGI and its participating customers organized a BGI Renewal Working Group to develop a process for securing a competitive replacement gas supply. A series of meetings with the Boundary customers was held to discuss the replacement of the gas deliveries at Niagara Falls once the original contract expired in January 2003.

Initially the Working Group chose to proceed with an Options/RFP Phase of the Renewal Project. This Phase would identify and review possible options for a replacement gas supply, and review the existing transportation capacity arrangements for gas deliveries from Niagara on the Tennessee Pipeline. This phased approach was designed to permit a discrete decision by each Boundary customer as to whether they wished to proceed to the Contract Phase.

The Boundary Renewal Working Group reviewed various aspects of the renewal process:

1. What were the participating LDCs looking for in a replacement supply?
2. How should an effective RFP on gas supply best be structured to secure a least cost supply?
3. What was required to renew the transportation capacity from Niagara to the LDC city gates on the Tennessee Gas Pipeline?

RFP PROCESS AND RESULTS

Q. Please describe the objective of the Request for Proposals (RFP) process.

A. The objective of the RFP process was to secure a reliable, market competitive replacement gas supply for interested BGI customers. The RFP process was launched in the Fall of 2001 in order to solicit, evaluate, and select, through a competitive bidding process, a successor source(s) of firm natural gas supply to replace the expiring supplies that BGI currently imports into the Northeast.

Q. Please describe the RFP timetable.

A. The RFP for replacement gas supply was issued on November 21, 2001 (see Exhibit FCD-4). The RFP was issued 14 months in advance of the contract expiry date of January 15, 2003 to allow sufficient time to address the gas supply renewal prior to expiration of the notice periods required for renewal of the Tennessee transportation contracts. The majority of the transportation contracts required that the shippers give the pipeline notice of their intention to renew one year in advance of the expiry, i.e., January 15, 2002. Responses to the RFP were due by December 20, 2001 to enable the evaluation of the RFPs prior to the decision on transportation contract renewal. The timetable for the RFP process was as follows:

Issue RFP to Supplier List	November 21, 2001
TGP Notification to FTA Shippers	December 14, 2001
RFP Response Deadline	December 20, 2001
BGI / Repurchaser Review of Bids	Dec. 20, 2001 – Jan 2, 2002
Selection of Short List Award Group	January 2, 2002
Bid Refresher with Award Group	January, 2002
Determine Winner	January 10, 2002
FTA Shippers Respond to TGP Notice	January 14, 2002
Repurchaser Commitment Date	February 1, 2002

Conclude Detailed Gas Contract	June 2002
Execute Contract	July 2002
Regulatory Reviews / Approvals	August 2002 – Jan. 15, 2003
Commence Contract Deliveries	January 15, 2003

Q. How were the qualified bidders identified?

A. Based on the experience that the Boundary LDCs and BGI have had with other RFP processes, the Boundary management team put together a list of qualified bidders, which was reviewed and approved by the Boundary LDCs as part of the RFP preparations. This list included many of the top 25 natural gas marketers[2] (by volume) as published in the November 30, 2001 GAS DAILY publication (see Exhibit FCD-5). The majority of the bidders were interviewed by the Boundary management team prior to issuing the RFP.

The Companies that were sent a bidders RFP package, and invited to bid on the Boundary replacement gas volumes, were:

Aquila Energy
BP Amoco
Coral Energy
Duke Energy
Dynegy
El Paso
Imperial Oil
Mirant

[2] Enron was dropped as a qualified bidder due to their financial difficulties surfacing at the time the RFP list was compiled.

PanCanadian Energy Services[3]
PG&E National Energy Group
Reliant Energy Services Canada
Sempra Energy Trading
Williams Energy Marketing & Trading.

Q. Please describe the terms of the RFP.

A. At the time of the issuance of the RFP, it was estimated that the replacement volumes would be in the 60,000 – 72,280 Decatherms per day (Dth/d) range, depending on the final commitments by the BGI customers. RFP bidders were encouraged to submit multiple volume options that would provide delivery flexibility. For example:

1. A bid based on 100% take, i.e., base load
2. A bid that includes first of the month flexibility

Based on the volatility of gas prices, regulatory uncertainties and their individual portfolio requirements in the energy market, BGI customers sought gas supply proposals for 14 months or 26 months. The term extended beyond a one year or a two year period to enable the end of the contract to coincide with the end of the winter season, i.e., March 31, 2004, or March 31, 2005.

Bidders were asked to submit bids with multiple pricing options such as:

1. NYMEX plus a fixed or floating basis
2. Gas priced at the delivery point, i.e. Niagara Monthly Index
3. Gas priced on a basket of fuels

[3] Subsequently merged with AEC Oil and Gas Company to form EnCana.

4. Other innovative pricing schemes that the bidder would propose

The RFP specified that commencement of and payment for gas service as contemplated by the RFP was subject to prior approval of state and federal regulatory agencies. Further, the RFP specified that BGI customers, including Bay State, were not obligated to enter into the resulting replacement supply contract.

Q. How did you arrive at the final list of qualified bids?

A. Of the thirteen RFP potential bidders, nine chose to reply and four did not. One of the nine submitted bids was so incomplete as to be non-responsive and therefore was eliminated from consideration. Exhibit FCD-6 provides each of the nine original bids. The following table shows the progression to the final list of eight bidders.

RFP Recipients (13)	RFP Bidders (9)	Incomplete Bids (1)	Qualified Bids (8)
1. Coral	1. A	1. H	1. A
2. El Paso	2. B		2. B
3. Aquila	3. C		3. C
4. Duke	4. D		4. D
5. Dynegy	5. E		5. E
6. BP	6. F		6. F
7. Imperial Oil	7. G		7. G
8. Mirant	8. H		8. I
9. PanCanadian	9. I		
10. PG&E			
11. Reliant			
12. Sempra			
13. Williams			

Q. How were the bids standardized for purposes of evaluation?

A. The standard services offered by the bidders included City-gate prices, Niagara, Dawn and Dracut index prices, NYMEX plus a fixed basis, NYMEX plus a floating basis, Tetco M3 prices, and prices based on a basket of fuels including #2 and #6 oils. The standardization involved looking at historic pricing relationships between Henry Hub and various delivery points and then using those relationships to convert all of the submitted prices to a NYMEX price. Page 1 of Exhibit FCD-7 provides the pricing assumptions/conversions required for each bidder while page 2 of Exhibit FCD-7 provides the conversion tables used to convert all bids to a NYMEX basis price.

Once all of the services were standardized to a NYMEX price, then they could be compared on the same basis. Next, the bids were separated into 2 groups: the 14-month term bids and the 26-month terms. Each of these term categories was further subdivided into the delivery points offered for that term, such as Niagara, Dracut and City-gate Services. Once the delivery point was established, then the bid was further subdivided into base load and swing flexibility options. Exhibit FCD-8 illustrates the sorting of the bids for comparative purposes.

Q. What were the non-price criteria used to evaluate the bids?

A. Consistent with Bay State's portfolio objectives and Department precedent, the bids were evaluated based on the non-price criteria of reliability/supply security, flexibility, and supplier viability. A detailed description of the elements within each of these criteria is contained in Exhibit FCD-9.

RFP Results

Q. Please describe how the bids were assessed.

A. After standardizing the price offered for all of the services, the bids were assessed in terms of four criteria previously mentioned and allocated maximum percentage values as follows:

Price of the service offered (30%)

Security of supply (35%)

Bid flexibility (20%)

Supplier viability (15%)

Q. What were the results of the scoring for non-price criteria?

A. On the basis of a possible 70 points for non-price criteria, the top three suppliers were EnCana/PanCanadian, Bidder B and Bidder D. A summary of the results and the detailed scoring for each criteria is provided in Exhibit FCD-10.

Q. What were the results on the pricing portion of the bid analysis?

A. After the standardization of all bids, it was determined, based on the total value over NYMEX,[4] that the overall bidder prices at Niagara were the most competitive. Of the bids at Niagara, the top three bidders were again, EnCana/PanCanadian, Bidder B and Bidder D. Exhibit FCD-11 provides the rankings of each of the service offerings under the four delivery options on a total value over NYMEX basis.

Q. What were the overall results of the RFP?

A. Using the previously discussed criteria and sorting sequence, EnCana/PanCanadian, Bidder B and Bidder D were very close to one another overall. Given that the winter in the Northeast had been mild, and the price of gas had declined significantly between the time the RFP was issued and the evaluation period, it was decided that the group would go back to the top three bidders and ask them to narrow the scope of their respective bids, focusing on Niagara-only deliveries and ask each of them to "refresh" their bids with respect to price in order for the BGI customers to take advantage of the low prices prevailing in the market.

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[4] The total value over NYMEX is determined by multiplying the volume bid times the standardized NYMEX basis price. In some instances, the bidder is not providing the full volumes requested in the RFP resulting in a lower total value over NYMEX result. These deficient bids are noted in Exhibit FCD-11.

The "refresher" bid statement provided as Exhibit FCD-12 was similar to the original RFP document. The narrowing of the bid included:

a) Flexibility Options	- either a 100% baseload option, or - a first of the month take or release flexibility on volume, or - a baseload in the winter and a first of the month take or release during the summer months.
b) Delivery Point	- Niagara only service - Bidders must describe supply source
c) Pricing Options	- NYMEX plus a fixed basis - Niagara price index

The updated bids, provided as Exhibit FCD-13, showed that EnCana/PanCanadian and Bidder B had very comparable bids. with EnCana's price being slightly lower and Bidder B's flexibility being better. Exhibit FCD-14 provides the rankings for all three bidders.

After clarifications and negotiations with EnCana and Bidder B, each entity provided a final bid for baseload, annual swing and summer-only swing service. As demonstrated in the rankings contained in Exhibit FCD-15, EnCana provided the lower bid for all three services and, thus, the Project working group selected EnCana as its Boundary replacement supplier.

Q. Why did Bay State elect the 26-month option for the EnCana supply?

A. The supply will enhance the reliability and price stability of Bay State's supply portfolio by offering a committed supply source at a known price over time. Overall, Bay State's gas supply purchases are largely made on the spot market; therefore, Bay State has substantial flexibility to adjust its supply purchases, as necessary, during the five-year transition period established by the Department in D.T.E. 98-32-B (1999). In addition, the contract terms offer Bay State significant flexibility to ratchet down its purchases from EnCana prior to the beginning of each month if a lower cost, reliable replacement supply is found or if the supply is not needed altogether.

SENDOUT ® Analysis

Q. Did Bay State perform an analysis of the supply options described previously utilizing its SENDOUT ® model?

A. Yes. Consistent with its approved planning process, the Company conducted an analysis on the full range of supply alternatives using its SENDOUT ® model.

Q. Please describe SENDOUT ® analysis.

A. The Company used a resource mix analysis, which allows SENDOUT ® to choose the appropriate maximum daily quantity ("MDQ") of a range of resource alternatives over a given time period that contribute to a least-cost portfolio. In this case, the planning horizon was from November 2002 through October 2005 in order to encompass the timeframe for Boundary replacement supply alternatives. The resource mix analysis was based on normal year requirements over the planning horizon. Further, the resources were compared on a 100% load factor basis in order to unitize the demand costs of each alternative since the MDQ varied by resource option and in order to properly account for unique demand costs associated with each supply alternative including firm pipeline transportation demand charges, reservation fees and, in the Boundary replacement options, a management services fee of $0.0128 per Dth.

The range of supply alternatives in the resource mix included the lowest price bids for each of delivery point (ENCANA, DRACUT/NIAG and CITYGATE) requested in the Boundary RFP and contained in Exhibit FCD-11, as well as the Company's El Paso Peaking contract (EL PASO CG) previously approved in Bay State Gas Company, D.T.E. 01-62 (2001), which will expire on March 1, 2003.

Q. What were the results of the SENDOUT ® analysis?

A. The SENDOUT ® model opted to take 100% of the available MDQ provided in the EnCana supply alternative while reducing its required MDQ for the El Paso Peaking contract. Page 13 of Exhibit FCD-16 summarizes the supply alternatives and the associated capacity segments and provides the maximum level MDQ available for each supply alternative and the resulting MDQ selected by SENDOUT ®.

Standard of Review

Q. Please describe the Department's standard of review.

A. The Department's standard of review for resources of this type involve three criteria that Bay State must meet: first, that Bay State employed least-cost planning techniques; second, that the acquisition compare favorably with respect to non-price characteristics such as reliability and flexibility; and third, that the acquisition is in the public interest. The public interest standard requires an LDC to demonstrate that the acquisition (1) is consistent with the company's portfolio objectives, and (2) compares favorably to the range of alternative options reasonably available to the company and its customers. See, Commonwealth Gas Company, D.P.U. 94-174-A, at 27 (1996).

Q. Has Bay State satisfied the Department's standard of review with its decision to contract with EnCana for the Boundary replacement supply?

A. Yes. In Bay State Gas Company, D.P.U. 93-129 (1996) ("D.P.U. 93-129") and D.T.E. 98-86, as well as in decisions approving specific resource acquisitions, D.P.U. 94-16, D.P.U. 94-16A and D.P.U. 95-87, Bay State's planning process has been reviewed by the Department. In these proceedings, the Department has repeatedly found that the Company's supply planning process is consistent with the Department' requirements. In D.P.U. 93-129, the Department summarized its earlier findings in the referenced proceedings approving resource acquisitions as follows:

> In those cases, the Department found that Bay State's supply planning goals and objectives, particularly its effort to procure a "best-cost" portfolio, were reasonable and appropriate, and that its flexible planning framework guided each particular acquisition process in a manner that built upon the Department's general objectives of reliability, flexibility, diversity and least-cost, while allowing Bay State the discretion to tailor its approach to the Company's particular needs.

Id., at 42.

The Department reiterated its approval of Bay State's resource planning process in its July 2000 Order on Bay State's most recent forecast and supply plan. Bay State Gas Company, D.T.E. 98-86 (2000). In that Order, the Department noted that Bay State's planning process maintains reliable, least-cost service for its firm customers, and that the Company's plans were reviewable, appropriate and reliable. D.T.E. 98-86, at 30. Therefore, based on findings in various proceedings, the Department has found Bay State's planning process to be reasonable and appropriate.

The first element of the Department's standard of review for replacement resources is an analysis of whether least-cost planning techniques were used in the decision-making process. The analysis performed by Bay State through its RFP process and through its SENDOUT ® model demonstrates that EnCana was the least-cost option available to Bay State among all viable alternatives. Therefore, Bay State's decision meets this element of the Department's standard as supported by the previously discussed RFP and SENDOUT ® model results.

Bay State's EnCana decision also satisfies the second element of the Department's standard of review. Specifically, the EnCana resource acquisition was consistently ranked at or near the top when compared to other supply bids on the basis of the non-price factors of reliability, flexibility and viability.

The third element of the Department's standard of review requires that the Company demonstrate that the EnCana resource acquisition is in the public interest. Bay State's decision-making process begins with the establishment of appropriate goals and objectives. The primary goal of Bay State's planning process is to acquire and manage resources in a manner that achieves a best-cost resource portfolio for its customers. A best-cost portfolio appropriately balances lower costs with other important criteria such as reliability and flexibility. Pursuit of a best-cost portfolio allows Bay State to provide its customers with reliable service at a reasonable cost. The Company's overall portfolio objective is supported by a number of specific resource planning objectives, which are summarized as follows:

(1) maintain portfolio reliability (which includes enhancing diversity across pipelines and supply basins);

(2) reduce portfolio costs;

(3) provide flexibility; and

(4) acquire viable resources.

Bay State's resource planning process employs analytic tools, such as SENDOUT ®, and assessment methods, such as the RFP bid evaluation process described previously, to perform short and long-range planning and to evaluate the individual resource decisions it must make. These tools and methods ensure that the planning process is thorough, and that it remains objective in its pursuit of a best-cost portfolio.

Bay State has demonstrated through its SENDOUT ® analysis and its RFP bid evaluation process that the EnCana resource option compares favorably to a range of alternative options on both a price and non-price basis and, thus contributes to the Company's objective of a best-cost portfolio.

Conclusion

Q. Please summarize your conclusions.

A. Bay State, through its participation in the Project working group, conducted a comprehensive RFP process in which it solicited bids for a replacement supply contract at various delivery points and from a wide range of market participants. The detailed analysis of those bids clearly demonstrated that EnCana had the best bid on both a price and non-price basis.

The Company, through the use of a resource mix analysis in its previously approved analytical tool, SENDOUT ®, confirmed that EnCana was a least-cost resource and contributed to the Company's goal of maintaining a least-cost portfolio.

The Company has also demonstrated that the EnCana resource decision satisfies the Department's standard of review as it applies to replacement supply contracts.

Q. Does this complete your prefiled direct testimony in this proceeding?

A. Yes, it does.